FILE COPY

Office-Supreme Court, U.S.
FILED
MAR 4 1959
JAMES R. BROWNING, Clerk

No. 682

In the Supreme Court of the United States

OCTOBER TERM, 1958

JOHN I. COOPER, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

J. LEE RANKIN,
Solicitor General,
CHARLES K. RICE,
Assistant Attorney General,
ROBERT N. ANDERSON,
JAMES P. TURNER,
Attorneys,
Department of Justice, Washington 25, D.C.

INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statute and regulations involved	2
Statement	2
Argument	5
Conclusion	7
Appendix	8

CITATIONS

Cases:	
Blair v. *Wilson Syndicate Trust*, 39 F. 2d 43	7
Cleveland Trust Co. v. *Commissioner*, 115 F. 2d 481	7
Commissioner v. *Guitar Trust Estate*, 72 F. 2d 544	7
Commissioner v. *Morriss R. Co. Trust No. 2*, 68 F. 2d 648	7
Corn Products Co. v. *Commissioner*, 350 U.S. 46	6
Helvering v. *Coleman-Gilbert*, 296 U.S. 369	5
Helvering v. *Combs*, 296 U.S. 365	5
Helvering v. *Washburn*, 99 F. 2d 478	7
Lewis & Co. v. *Commissioner*, 301 U.S. 385	5, 7
Morrissey v. *Commissioner*, 296 U.S. 344	5
Nee v. *Main Street Bank*, 174 F. 2d 425	7
Pennsylvania Co., Etc. v. *United States*, 146 F. 2d 392	7
Porter v. *Commissioner*, 130 F. 2d 276	7
Swanson v. *Commissioner*, 296 U.S. 362	5
United States v. *Davidson*, 115 F. 2d 799	7
United States v. *Rayburn*, 91 F. 2d 162	7
Statute:	
Internal Revenue Code of 1939, Sec. 3797 (a) (26 U.S.C. 1952 ed., Sec. 3797(a))	2, 5, 8
Miscellaneous:	
Treasury Regulations 111:	
Sec. 29.3797-1	2, 8
Sec. 29.3797-2	2, 9
Sec. 29.3797-3	2, 5, 9
Treasury Regulations 118:	
Sec. 39.3797-1	8
Sec. 39.3797-2	8
Sec. 39.3797-3	8

In the Supreme Court of the United States

OCTOBER TERM, 1958

No. 682

JOHN I. COOPER, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum findings of fact and opinion of the Tax Court (R. 46–56) are not officially reported. The opinion of the Court of Appeals (Pet. A1–A10) is not yet officially reported.

JURISDICTION

The judgment of the Court of Appeals was entered on November 28, 1958. The petition for rehearing was denied on December 29, 1958. The petition for a writ of certiorari was filed on February 3, 1959. The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254(1).

QUESTION PRESENTED

Whether the taxpayer trust was an association taxable as a corporation under Section 3797(a)(3) of the Internal Revenue Code of 1939.

STATUTE AND REGULATIONS INVOLVED

The pertinent provisions of Section 3797(a) of the Internal Revenue Code of 1939 and Sections 29.3797–1, 29.3797–2 and 29.3797–3 of Treasury Regulations 111 are printed in the Appendix, *infra*, pp. 8–12.

STATEMENT

The facts, found by the Tax Court (R. 47–52), and stated by the Court of Appeals (Pet. A1–A7), are in large part undisputed and may be summarized as follows:

The taxpayer trust filed fiduciary income tax returns for the years 1950 to 1953 inclusive. The Commissioner determined deficiencies for each of these years on the ground that the taxpayer trust was an association taxable as a corporation under Section 3797(a)(3) of the Internal Revenue Code of 1939. (Pet. A2.)

In 1914, the will of John M. Cooper created a testamentary trust of the entire residue of the testator's estate. This trust was to last for a term of 35 years with distribution at the end of that period in equal shares to the testator's children then living and to the heirs of his deceased children. On October 19, 1949, the assets of this trust having an aggregate value of $355,323 were distributed. They consisted of cash, real estate, a controlling interest of 315 shares

of the Baxter State Bank, and United States Series G Bonds. Also on October 19, 1949, the instrument creating the taxpayer trust was executed by the beneficiaries of the testamentary trust and their wives. This instrument conveyed to two of the beneficiaries, John I. Cooper and H. W. Price, as trustees, all the assets of the testamentary trust, except the cash and Series G bonds. (Pet. A2.)

The instrument creating the taxpayer trust recited that the property described therein had "an income producing potential" which could "be better protected by a unified control, management and operation * * * until such time as the trustees * * * or their successors" should "sell and convert into cash" the assets of the trust or any part thereof "for distribution among the grantors." (Pet. A3; R. 18.)

The term of the trust was fixed at ten years. Broad powers and duties were conferred on the trustees including, *inter alia*, full control of the trust property with discretionary power to sell, lease, mortgage or pledge any or all of the assets, and the power to borrow money and to invest the trust funds. The stated purposes of the trust included the "economical and centralized management and operation of the property" until liquidation and distribution, and "the holding together" of the property so that the "maximum return" from rentals, royalties and sales could be achieved. In the event the trust assets had not been distributed at the end of the term, the trustees were authorized to make distribution in cash or in kind. Quarterly distributions of $2,000 were required in the instrument, but such distributions

could be increased in the discretion of the trustees if "such additional funds can be distributed without impairing the continued normal and economical administration of the trust." Continuity of the trust was insured since the interests of the beneficiaries were transferable; the heirs or devisees of a deceased beneficiary succeeded to his interest; and, provision was made for successor trustees upon the death or resignation of a trustee. In fact, one of the trustees died in 1951 and was succeeded by L. W. Price, and certain beneficiaries have died and have been succeeded by their heirs or assigns. (Pet. A3–A5).

The trust real estate consisted primarily of farm lands which were rented on a share-crop basis. Two sales of real estate during 1951 and 1952 resulted in a gain of $4,686.40 and a loss of $4,600, respectively. The real property also included two tracts under mineral lease. At their expiration, the trustees executed new leases on each tract. One lease was for a period of ten years from 1953 and thus extended well beyond the terminal date of the trust. (Pet. A5–A6)

The 315 shares of stock in the Baxter State Bank represented a controlling interest in the bank. Several sales of stock were made to valued customers and employees, but control of the bank was retained by the trust. (Pet. A6,)

Large profits were made by the trust through these business activities. Earnings were received from share-crop rentals, mineral royalties, and dividends. Substantial amounts of cash were on hand at the end of each of the taxable years. (Pet. A6, A9)

Based on the foregoing, the Tax Court (R. 52) and the Court of Appeals (Pet. A10) both concluded that the taxpayer trust was formed for the purpose of carrying on a business enterprise and was, for each of the years in question, an association, taxable as a corporation.

ARGUMENT

The decision below correctly applies well settled rules of law to basically undisputed facts. This Court has considered the problems of treating trusts as associations under the taxing statutes in a number of cases and the applicable legal principles are now well established. *Morrissey* v. *Commissioner,* 296 U.S. 344; *Swanson* v. *Commissioner,* 296 U.S. 362; *Helvering* v. *Combs,* 296 U.S. 365; *Helvering* v. *Coleman-Gilbert,* 296 U.S. 369; and, *Lewis & Co.* v. *Commissioner,* 301 U.S. 385.

Section 3797(a)(3) of the Internal Revenue Code of 1939, Appendix, *infra,* p. 8, defines the term "corporation," when used in the Code, as including "associations." It is settled by the decisions that trusts which are engaged in carrying on a business for profit and which have the essential characteristics of an association will be taxed as a corporation under this provision. Conversely, where the trust is an ordinary trust "created by will or by declaration of the trustees or the grantor, the trustees of which take title to the property for the purpose of protecting or conserving it * * *", it will not be taxed as an association. Regulations 111, Section 29.3797-3, Appendix, *infra,* pp. 9-12; see also *Lewis & Co.* v. *Commissioner; supra.*

Whether a particular trust falls within the category of an association, as that term has been defined, is a question of fact in each case, inappropriate for review here. *Corn Products Co.* v. *Commissioner*, 350 U.S. 46, 51.

The opinions below clearly indicate that the Tax Court and the Court of Appeals correctly understood and applied the above rules. Moreover, there is abundant factual support for the conclusion that the taxpayer trust had the requisite form and purpose for classification as an association. That the primary purpose of the trust was the conduct of business and not the liquidation of family assets is shown by the recitations in the trust instrument itself quoted above; the broad, business-like powers granted the trustees; the fact that liquidation was neither required nor attempted; and the further fact that all the activities of the trustees reflect a profit producing, not a liquidating, motive. (Pet. A9.) There is also the necessary resemblance to corporate form since the instrument provides for a centralized management and a continuing entity, continuity regardless of death among beneficiaries, and a means for transfer of the beneficial interests. (Pet. A8–A9.)

The cases cited as being in conflict with the opinion below (Pet. 9–10) are distinguishable on their facts. For example, in some the requisite business activity was absent. *Blair* v. *Wilson Syndicate Trust*, 39 F. 2d 43, 46 (C.A. 5th); *Cleveland Trust Co.* v. *Commissioner*, 115 F. 2d 481, 484 (C.A. 6th); *Pennsylvania Co., Etc.* v. *United States*, 146 F. 2d 392, 396 (C.A. 3d); *Helvering* v. *Washburn*, 99 F. 2d 478, 481 (C.A. 8th). In

others, there was no resemblance to an association. *United States* v. *Davidson*, 115 F. 2d 799, 801 (C.A. 6th); *Lewis & Co.* v. *Commissioner*, *supra*. And, in some all of the attendant circumstances indicated that an ordinary liquidating or family trust was involved. *Blair* v. *Wilson Syndicate Trust*, *supra*; *Commissioner* v. *Morriss R. Co. Trust No. 2*, 68 F. 2d 648, 651 (C.A. 7th); *Commissioner* v. *Guitar Trust Estate*, 72 F. 2d 544 (C.A. 5th).

Indeed, some of the cases cited as conflicting with the opinion below held that the trusts involved were taxable as associations because the requisite form and activity were present. *Nee* v. *Main Street Bank*, 174 F. 2d 425 (C.A. 8th); *Porter* v. *Commissioner*, 130 F. 2d 276 (C.A. 9th); *United States* v. *Rayburn*, 91 F. 2d 162 (C.A. 8th).

CONCLUSION

The petition for writ of certiorari should be denied.

Respectfully submitted.

J. LEE RANKIN,
Solicitor General.
CHARLES K. RICE,
Assistant Attorney General.
ROBERT N. ANDERSON,
JAMES P. TURNER,
Attorneys.

MARCH 1959.

APPENDIX

Internal Revenue Code of 1939:

SEC. 3797. DEFINITIONS.

(a) When used in this title, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof—

* * * * * *

(3) *Corporation.*—The term "corporation" includes associations, joint-stock companies, and insurance companies.

* * * * * *

(26 U.S.C. 1952 ed., Sec. 3797.)

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939: [1]

SEC. 29.3797–1. *Classification of Taxables.*—For the purpose of taxation the Internal Revenue Code makes its own classification and prescribes its own standards of classification. Local law is of no importance in this connection. Thus, a trust may be classed as a trust or as an association (and, therefore, as a corporation), depending upon its nature or its activities. (See section 29.3797–3.) * * * The term "corporation" is not limited to the artificial entity usually known as a corporation, but includes also an association, a trust classed as an association because of its nature or its activities, a joint-stock company, an insurance company, and certain kinds of partnerships. (See sections 29.3797–2 and 29.3797–4.) The definitions, terms, and classifications, as set forth in

[1] The substantially similar provisions of Regulations 118, Secs. 39.3797–1, 39.3797–2 and 39.3797–3, apply to the taxable years 1952 and 1953 and are not reproduced herein.

section 3797, shall have the same respective meaning and scope in these regulations.

SEC. 29.3797-2 [as amended by T.D. 5468, 1945 Cum. Bull. 332]. *Association.*—The term "association" is not used in the Internal Revenue Code in any narrow or technical sense. It includes any organization, created for the transaction of designated affairs, or the attainment of some object, which, like a corporation, continues notwithstanding that its members or participants change, and the affairs of which, like corporate affairs, are conducted by a single individual, a committee, a board, or some other group, acting in a representative capacity. It is immaterial whether such organization is created by an agreement, a declaration of trust, a statute, or otherwise. It includes a voluntary association, a joint-stock association or company, a "business" trust, a "Massachusetts" trust, a "common law" trust, an inter-insurance exchange operating through an attorney in fact, a partnership association, and any other type of organization (by whatever name known) which is not, within the meaning of the Code, a trust or an estate, or a partnership. An "investment" trust of the type commonly known as a management trust is an association, and a trust of the type commonly known as a fixed investment trust is an association if there is power under the trust agreement to vary the investment of the certificate holders. (See *Commissioner* v. *North American Bond Trust,* 122 Fed. (2d) 545, certiorari denied, 314 U.S. 701.) If the conduct of the affairs of a corporation continues after the expiration of its charter, or the termination of its existence, it becomes an association.

SEC. 29.3797-3. *Association Distinguished from Trust.*—The term "trust", as used in the Internal Revenue Code, refers to an ordinary trust, namely, one created by will or by declaration of the trustees or the grantor, the

trustees of which take title to the property for the purpose of protecting or conserving it as customarily required under the ordinary rules applied in chancery and probate courts. The beneficiaries of such a trust generally do no more than accept the benefits thereof and are not the voluntary planners or creators of the trust arrangement. Even though the beneficiaries do create such a trust, it is ordinarily done to conserve the trust property without undertaking any activity not strictly necessary to the attainment of that object.

As distinguished from the ordinary trust described in the preceding paragraph there is an arrangement whereby the legal title to the property is conveyed to trustees (or a trustee) who, under a declaration or agreement of trust, hold and manage the property with a view to income or profit for the benefit of beneficiaries. Such an arrangement is designed (whether expressly or otherwise) to afford a medium whereby an income or profit-seeking activity may be carried on through a substitute for an organization such as a voluntary association or a joint-stock company or a corporation, thus obtaining the advantages of those forms of organization without their disadvantages. The nature and purpose of a cooperative undertaking will differentiate it from an ordinary trust. The purpose will not be considered narrower than that which is formally set forth in the instrument under which the activities of the trust are conducted.

If a trust is an undertaking or arrangement conducted for income or profit, the capital or property of the trust being supplied by the beneficiaries, and if the trustees or other designated persons are, in effect, the managers of the undertaking or arrangement, whether the beneficiaries do or do not appoint or control them, the beneficiaries are to be treated as voluntarily joining or cooperating with each

other in the trust, just as do members of an association, and the undertaking or arrangement is deemed to be an association classified by the Internal Revenue Code as a corporation. However, the fact that the capital or property of the trust is not supplied by the beneficiaries is not sufficient reason in itself for classifying the arrangement as an ordinary trust rather than as an association.

By means of such a trust the disadvantages of an ordinary partnership are avoided, and the trust form affords the advantages of unity of management and continuity of existence which are characteristic of both associations and corporations. This trust form also affords the advantages of capacity, as a unit, to acquire, hold, and dispose of property and the ability to sue and be sued by strangers or members, which are characteristic of a corporation; and also frequently affords the limitation of liability and other advantages characteristic of a corporation. These advantages which the trust form provides are frequently referred to as resemblance to the general form, mode of procedure, or effectiveness in action, of an association or a corporation, or as "quasi-corporate form." The effectiveness in action in the case of a trust or of a corporation does not depend upon technical arrangements or devices such as the appointment or election of a president, secretary, treasurer, or other "officer," the use of a "seal," the issuance of certificates to the beneficiaries, the holding of meetings by managers or beneficiaries, the use of a "charter" or "by-laws," the existence of "control" by the beneficiaries over the affairs of the organization, or upon other minor elements. They serve to emphasize the fact that an organization possessing them should be treated as a corporation, but they are not essential to such classification, for the fundamental benefits enjoyed by a corporation, as outlined above, are

attained, in the case of a trust, by the use of the trust form *itself*. The Internal Revenue Code disregards the technical distinction between a trust agreement (or declaration) and ordinary articles of association or a corporate charter, and all other differences of detail. It treats such a trust according to its essential nature, namely, as an association. This is true whether the beneficiaries form the trust or, by purchase or otherwise, acquire an interest in an existing trust.

The mere size or amount of capital invested in the trust is of no importance. Sometimes the activity of the trust is a small venture or enterprise, such as the division and sale of a parcel of land, the erection of a building, or the care and rental of an office building or apartment house; sometimes the activity is a trade or business on a much larger scale. The distinction is that between the activity or purpose for which an ordinary strict trust of the traditional type would be created, and the activity or purpose for which a corporation for profit might have been formed.